

The ILLINOIS Funds

Prime Fund

Investment Policy

1.0 Policy: The State Treasurer of Illinois has authority under Section 17 of the State Treasurer's Act (15 ILCS 505/17) to establish and administer an investment pool to supplement and enhance investment opportunities otherwise available to managers of public funds or public agencies in the state. The Treasurer may invest the assets of the investment pool in the same types of investments and subject to the same limitations provided for the investment of funds in the State Treasury. This policy specifically addresses The Illinois Funds Prime Fund. The Prime Fund will provide opportunities for public agencies to invest in a fund that has been rated AAAM by Standard & Poor's and also has the potential to generate enhanced return for public investors. This is accomplished by requiring a 30-day minimum deposit, by investing more funds in high quality instruments with a relatively higher return and maintaining a maximum weighted average portfolio maturity of 60 days.

2.0 Objective: The primary objectives of The Prime Fund are to invest public funds with a more long-term objective than the Illinois Funds Money Market Fund and create opportunities for enhanced investment return for public investors in the State of Illinois. The Fund has a AAAM rating from Standard & Poor's, which is the best rating available for a Local Government Investment Pool. The AAAM rating ensures that investments are placed only in the highest quality investments.

2.1 Safety: The safety of principal is one of the main objectives of the investment program. Prime Fund investments will be undertaken in a manner which seeks to ensure the preservation of principal in the portfolio while providing enhanced return. To obtain this objective, diversification among permissible investments is required to ensure that The Prime Fund properly manages market, interest rate and credit risk.

2.2 Liquidity: The investment portfolio will remain sufficiently liquid to enable The Prime Fund to meet all participant redemption demands that might be reasonably anticipated.

2.3 Return on Investment: The investment portfolio will be designed to obtain an enhanced return by requiring a minimum of 30 days for each deposit, a seven day notice for any withdrawal, and reasonable penalties for early withdrawal of funds prior to the expiration of the 30 day minimum and/or seven day notice period.

The Treasurer will select accepted industry benchmarks which best reflect The Prime Fund's portfolio and measure performance against certain benchmarks over time. The Treasurer will periodically review benchmarks for suitability.

3.0 Ethics and Conflicts of Interest: Authorized investment staff and employees in policy making positions for The Prime Fund will refrain from personal business activity that conflicts with proper execution of the investment program, or which impairs their ability to make impartial investment decisions. Such individuals will disclose to the Treasurer any material financial interests in financial institutions or broker/dealers that conduct business within the State. They will further disclose any personal investments that are related to the performance of The Prime Fund's portfolio. In addition, such individuals will subordinate their personal investment transactions to those of The Prime Fund, particularly with regard to the time of purchase and sales.

4.0 Authorized Broker/Dealers and Financial Institutions: Authorized investment staff will utilize the Treasurer's approved list of broker/dealers and financial institutions when selecting institutions to provide investment services.

In addition, a list will be maintained of approved security broker/dealers selected according to their creditworthiness, and their financial significance in the State. Broker/dealers will be evaluated on the basis of the location of their corporate office and the extent to which the broker/dealer has a labor or economic impact on the State. This list may include "primary" dealers or regional dealers that qualify under Securities and Exchange Commission Rule 15C3-1 (uniform net capital rule).

All financial institutions and broker/dealers interested in becoming qualified parties for investment transactions must supply the Treasurer's authorized investment staff with the following or equivalent acceptable to the Treasurer, where applicable:

- audited financial statements
- proof of National Association of Security Dealers certification
- trading resolutions
- proof of registration in the State of Illinois
- completed broker/dealer questionnaire
- certification of having read The Prime Fund's investment policy
- depository contracts
- published reports from rating agencies for brokers with investment grade ratings
- proof of emerging broker status
- Consolidated Reports of Condition and Income

An annual review of the financial condition and registration of qualified parties and investments will be conducted by the Treasurer's authorized investment staff. More frequent reviews may be conducted.

A current audited financial statement or equivalent acceptable to the Treasurer is required to be on file for each financial institution and broker/dealer with which The Prime Fund establishes a depository, trading, or safekeeping relationship. Qualified parties will submit updated financial statements or equivalent acceptable to the Treasurer when a material change in any of the above occurs.

5.0 Authorized and Suitable Investments: The following investments are permitted investments of state funds according to the Deposit of State Moneys Act (15 ILCS 520/22.5) and the Public Funds Investment Act (30 ILCS 235/2) and are authorized to the extent they are approved by Standard & Poor's for AAAM rated funds:

- In bonds, notes, certificates of indebtedness, treasury bills or other securities now or hereafter issued, which are guaranteed by the full faith and credit of the United States of America as to principal and interest; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5)
- In bonds, notes, debentures, or similar obligations of the United States of America or its agencies; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5)
- Repurchase agreements of government securities having the meaning set out in the Government Securities Act of 1986 subject to the provisions of that Act and the regulations issues thereunder; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5)
- In short term obligations of corporations organized in the United States with assets exceeding \$500,000,000 if (i) such obligations are rated at the time of purchase at one of the 2 highest classifications established by at least 2 standard rating services and which mature not later than 180 days from the date of purchase, (ii) such purchases do not exceed

10% of the corporations outstanding obligations, and (iii) no more than one-third of the public agency's funds may be invested in short term obligations of corporations

- The Public Treasurers' Investment Pool created under Section 17 of the State Treasurer Act; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5)
- In money market mutual funds registered under the Investment Company Act of 1940, provided the portfolio of any such money market mutual fund is limited to United States Treasury and United States Agency Securities and agreements to repurchase such obligations provided the funds are rated AAA; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5)
- Bonds, notes, debentures, or similar obligations of a foreign government, other than the Republic of Sudan, that are guaranteed by the full faith and credit of that government as to principal and interest, but only if the foreign government has not defaulted and has met its payment obligations for a period of at least 25 years immediately before the time of acquiring those obligations; Deposit of State Moneys Act (15 ILCS 520/22.5)
- Bonds issued by counties or municipal corporations of the State of Illinois; Deposit of State Moneys Act (15 ILCS 520/22.5)
- Interest bearing savings accounts, interest-bearing certificates of deposits or interest bearing time deposits or any other investments constituting direct obligations of any bank as defined by the Illinois Banking Act(205 ILCS 5/1 et seq.); Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5)

Suitable securities in the Prime Funds portfolio may be lent in accordance with the Federal Financial Institution Examination Council Guidelines.

6.0 Investment Restrictions: The following restrictions will apply to all Prime Fund investment transactions:

- Investments in derivative products and leveraging of assets through reverse repurchase agreements are prohibited.
- Repurchase agreements may only be executed with financial institutions or broker/dealers meeting the Treasurer's standards, which will include mutual execution of a Master Repurchase Agreement adopted by the Treasurer.
- There will be no investments in mortgage-backed securities of any kind.
- There will be no investments in asset-backed securities of any kind.
- There will be no investments in Bankers' Acceptances of any kind.

7.0 Collateralization: All Prime Fund deposits and repurchase agreements shall be secured by direct U.S. Treasury and/or U.S. Agency obligations as required by the Treasurer and provided for by the Deposit of State Moneys Act (15 ILCS 520) and the Treasurer's Acceptable Collateral Listing, which may change from time to time.

8.0 Safekeeping and Custody: All direct treasury, agency and instrumentality security transactions entered into by The Prime Fund will be conducted on a delivery-versus-payment (DVP) or receipt-versus-payment (RVP) basis. Securities will be held by a safekeeping agent

designated by the Treasurer, and evidenced by safekeeping receipts. Commercial Paper will settle daily with the Depository Trust Company.

9.0 Diversification: The primary purpose of diversification in general is to control credit and market risk. The Prime Fund portfolio will be diversified to eliminate the risk of loss resulting from concentration of assets in a specific maturity, a specific issuer or a specific class of securities. The majority of Prime Fund investments will be in direct obligations of the United States Treasury and United States Government Agencies and Instrumentalities as listed in section 5.0. In order to properly manage any risk that may be attendant to the investment of Prime Fund assets, The Prime Fund portfolio will observe the following diversification limits:

- The Prime Fund will invest no more than 50 percent of its total assets in securities with maturities greater than 30 days issued by any single permissible United States Government Agency or Instrumentality.
- The Prime Fund will invest no more than 5 percent of its total assets in securities issued by any single Commercial Paper Issuer (calculated at the time of purchase).
- A maximum of 33.3 percent of the portfolio may be invested in direct Commercial Paper Obligations not to exceed 180 days to maturity.
- A maximum of 25 percent of total assets may be invested in any approved AAAM Money Market Fund.

The Prime Fund will seek to achieve diversification in the portfolio by reasonably distributing investments within authorized investment categories, issuers and broker/dealers.

10.0 Internal Controls: The Treasurer will establish a system of internal controls, which will be documented in writing and filed with the Inspector General of the Treasurer's Office for review as an adjunct to the annual independent examination of the financial statements of The Prime Fund. The controls will be designed to prevent loss of public funds arising from fraud, employee error, misrepresentation by third parties, unanticipated changes in financial markets or imprudent actions by authorized investment staff of The Prime Fund. The Treasurer will publish the current investment policy annually in a newspaper of general circulation in both Springfield and Chicago.

11.0 Asset Allocation: The Treasurer shall approve asset allocation among investment categories authorized under Section 5.0 of this Investment Policy.

12.0 Competitive Bidding: Authorized investment staff will obtain competitive bids from at least three broker/dealers prior to executing repurchase agreements, purchasing United States Treasury securities, United States Government Agency or Instrumentality securities or Commercial Paper from a broker/dealer. Notwithstanding the foregoing, authorized investment staff may tender bids directly through a single broker/dealer for the original auction of individual U.S. Treasury obligations without obtaining competitive bids.

13.0 Liability: Authorized investment staff, acting in accordance with written procedures and this investment policy and exercising due diligence, will be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments. The Treasurer is bonded to a level of \$150,000 for the faithful performance of duties in relation to The Illinois Funds.

14.0 Reporting: A quarterly report will be presented by the Director of The Illinois Funds to the Treasurer and the Treasurer's Investment Policy Committee (listing of committee members attached). The quarterly report will contain the following:

- performance as compared to established benchmarks
- asset allocation
- any deviation from the standards established in Section 9.0 above
- any change in investment policy adopted during the quarter
- the weighted portfolio average days to maturity

An external audit listing all securities marked to market will be provided to the Treasurer and all participants annually.